

General Information Letter: Nexus determinations cannot generally be made by letter ruling.

December 20, 2002

Dear:

Your letter has recently been forwarded to the Income Tax Division of Legal Services for reply. It is my understanding that the Sales Tax Division has already responded to the sales tax issues in your August 27, 2002 letter. Your letter states as follows:

COMPANY, LLC is a public accounting firm in CITY, Ohio. We represent a client who has operations as described below. We are in the process of determining the client's corporate tax and sales tax filing requirements in certain states. We are writing to you for clarification of your states filing requirements, if any for our client.

Description of Services

Our client provides mystery shopping services for major corporations. They do not sell any products or tangible goods, they simply provide services. In addition, all of the mystery shopping services are performed by independent contractors and are paid accordingly. Ohio is the only state in which our client employs personnel. All services in your state are performed by independent contractors. In addition, our client only engages an independent contractor in your state very few times a year, sometimes as few as one time.

We are trying to determine the following:

1. Does our client have Nexus in your state?
2. Does the situation change if the headquarters of the corporation that has employed our client is located in that state?
3. What filing requirements, if any, does my client have with regards to your corporate tax?
4. What filing requirements, if any, does my client have with regards to your sales tax?

According to the Department of Revenue ("Department") regulations, the Department may issue only two types of letter rulings: Private Letter Rulings ("PLR") and General Information Letters ("GIL"). The regulations explaining these two types of rulings issued by the Department can be found in 2 Ill.Adm.Code §1200, or on the website <http://www.revenue.state.il.us/legalinformation/regs/part1200>.

Your first question relates to nexus. The question of nexus is highly fact-dependent. Therefore, the Department does not issue rulings regarding whether a taxpayer has nexus with the State. Such a determination can only be made in the context of an audit where a Department auditor has access to all relevant facts and circumstances.

Due to the nature of your inquiry and the information presented in your letter, we are required to respond with a GIL. GILs are designed to provide background information on specific topics. GILs, however, are not binding on the Department.

Section 201 of the Illinois Income Tax Act ("IITA"), 35 ILCS 5/101 et seq, imposes a tax measured by net income on corporations for the privilege of earning or receiving income in this State. The Due Process and Commerce Clauses of the Federal Constitution limit the power of States to subject foreign corporations to tax. The Due Process Clause requires that there exist some minimum connection between a state and the person, property, or transaction it seeks to tax (Quill Corp. v. North Dakota, 504 U.S. 298, 112 S.Ct. 1904 (1992)). Similarly, the Commerce Clause requires that the tax be applied to an activity with a substantial nexus with the taxing state. Id.

It is generally beyond the scope of a letter ruling to give precise guidance on nexus issues. However, the facts recited in your request indicate that your client might not apportion any income to Illinois even if it does have nexus. Based on the information in your letter, IITA Section 304(a)(3)(C) is most applicable to your client's situation. Accordingly, a more pertinent question is whether your client has income producing activity in Illinois. Section 304(a)(3)(C) states as follows:

- (C) Sales, other than sales governed by paragraphs (B) and (B-1), are in this State if:
 - (i) The income-producing activity is performed both within and without this State and a greater proportion of the income-producing activity is performed within this State than without this State, based on performance costs; or
 - (ii) The income-producing activity is performed both within and without this State and a greater proportion of the income-producing activity is performed within this State than without this State based on performance costs.

Enclosed please find a copy of IITA Section 304 along with a copy of 86 Ill.Adm.Code Section 100.3370. The Illinois Department of Revenue regulation 100.3370 defines "income producing activity" in subsection (c)(3). In particular, subsection (c)(3)(A) provides that activities of an independent third party – such as the shoppers in this case – are not considered "income producing activities" of the taxpayer. For your convenience, I have marked the appropriate section for you.

Your second question asks whether the situation changes if the headquarters of the corporation that employs your client is located in Illinois. If your client correctly falls under 304(a)(3)(C), the situation does not change since the determining factor is the income producing activities based on the enclosed Illinois regulation, 86 Ill.Adm.Code Section 100.3370.

Your last income tax question relates to our corporate tax filing requirements. Section 502(a) of the IITA describes when an Illinois income tax return is required. Pursuant to Section 501(a), an Illinois income tax return is required in two situations. The first situation is when a taxpayer is liable for Illinois income tax. The second situation is, in the case of a corporation qualified to do business in Illinois, when the taxpayer is required to file a federal income tax return, regardless of whether such person is liable for Illinois income tax.

As stated above, this is a general information letter which does not constitute a statement of policy that either applies, interprets or prescribes tax law. It is not binding on the Department.

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Sincerely,

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